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No. 02-1196

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 2002

THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION,

Appellant,

AGAINST

ETS PAYPHONES, INC.
AND
CHARLES E. EDWARDS,

Appellees.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

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BRIEF FOR PUBLIC INVESTORS ARBITRATION BAR ASSOCIATION, INC. AS AMICUS CURIAE IN SUPPORT OF THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION

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March 14, 2003

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March 14, 2003

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE IN SUPPORT OF THE SEC'S PETITION FOR WRIT OF CERTIORARI AND BRIEF AMICUS CURIAE IN SUPPORT THEREOF

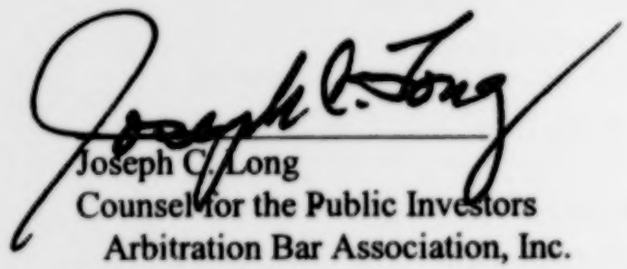
The Public Investors Arbitration Bar Association, Inc. ("PIABA") is a national non-profit voluntary public bar association with a membership of some 550 attorneys. In order to be a member of PIABA, an attorney must devote a significant portion of his or her practice to representing public investors (non-industry members) in private arbitrations involving securities matters. PIABA hereby respectfully moves for leave to file the attached brief, as **Amicus Curiae**, in the present case. Permission of the appellant, the United States Solicitor General, has been obtained. Permission of Charles E. Edwards, appellee, was sought and denied.

The interest of PIABA in this case arises from the fact that a number of members are involved in private arbitrations where hundreds of investors purchased ETS investments or similar interests in payphones offered by other companies. The decision of this Court could strongly influence the outcome of these future arbitrations.

Beyond the issue of whether payphones schemes involve the sale of securities in the form of investment contracts, this Court's decision will impact a number of other similar investments presently being offered to the public. These investments include automated teller machines, credit card processing units, and Internet access terminals, among others. None of the interests in these schemes are registered as securities and many are fraudulent. If the decision of the Eleventh Circuit is allowed to stand, the payphone and the other major schemes will go largely unregulated. Further, the public investors will be denied in the information and protection which the state and federal securities acts were designed to provide.

The focus of the brief of the Solicitor General on behalf of the Securities and Exchange Commission accompanying the petition for certiorari is limited to the Eleventh Circuit's analysis of the ETS payphone operation and its implications decision on the federal securities acts. The brief, which PIABA as **Amicus Curiae** seeks permission to file, will, however, have a wider focus. It will address the impact of this Court's decision on arbitration, state securities laws, and other types of similar schemes. It will provide the Court with an understanding of the potential impact that the Court's decision will have in these broader areas.

Respectfully submitted,



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March 14, 2003

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In the
Supreme Court of the United States
October Term, 2002

The United States Securities and Exchange Commission,

Appellant,

against

ETS Payphones, Inc.
and
Charles E. Edwards,

Appellees.

On Petition for Writ of Certiorari to
the United States Court of Appeals
for the Eleventh Circuit
Brief for the Public Investors Arbitration
Bar Association, Inc., as Amicus Curiae

INTEREST OF THE AMICUS CURIAE

The Public Investors Arbitration Bar Association, Inc. ("PIABA") is a national non-profit voluntary public bar association with a membership of some 550 attorneys.[1] In order to be a member of PIABA, an attorney must devote a significant portion of his or her practice to representing public investors (non-industry members) in private arbitrations involving securities matters.

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[1]Joseph C. Long, a member of PIABA and the undersigned counsel for PIABA, wrote the entire brief. No one other than PIABA, the amicus curiae, has made a monetary contribution to the preparation or submission of this brief.

The interest of PIABA in this case arises from the fact that a number of members are involved in private arbitrations where hundreds of investors purchased ETS investments or similar interests in payphones offered by other companies. The decision of this Court could strongly influence the outcome of these future arbitrations.

Beyond the issue of whether payphones schemes involve the sale of securities in the form of investment contracts, this Court's decision will impact a number of other similar investments presently being offered to the public. These investments include automated teller machines, credit card processing units, and Internet access terminals, among others. None of the interests in these schemes are registered as securities and many are fraudulent. If the decision of the Eleventh Circuit is allowed to stand, the payphone and the other major schemes will go largely unregulated. Further, the public investors will be denied the information and protection which the state and federal securities acts were designed to provide.

SUMMARY OF ARGUMENT

The Writ of Certiorari should be granted for four reasons. First, the question of national public interest in that it effects the definition of profits under the investment contract test in the federal and state securities acts. Second, the present decisions of this Court on this issue are ambiguous and need to be clarified. Third, the decisions of the various Courts of Appeals on the issue of "profits" are badly divided. Finally, the decision of the Eleventh Circuit is in conflict with the position of the SEC, the state courts under similar definitions in the state securities acts, and the state securities agencies themselves.

ARGUMENT

POINT I

THE ISSUE IN THIS CASE INVOLVES GREAT NATIONAL PUBLIC INTEREST AND, THEREFORE, SHOULD BE REVIEWED BY THIS COURT

PIABA believes the SEC has greatly understated the issue in the present case. The real issue is whether any debt security or contract requiring the payment of a fixed return can be an investment contract under the statutory definition of a "security" in either the Securities Act of 1933[2] or the Exchange Act of 1934.[3] The Eleventh Circuit, in the present case, interpreted this Court's decision in *United Housing Foundation v. Forman*, 421 U.S. 837 (1975), defining the "profit" element of *Howey*[4] test for investment contracts to exclude either the payment of interest or contract fixed return obligations. It reached this conclusion based upon its reading of *United Housing* to require that the investor's profit must come from the earnings of the enterprise. Interest or fixed return contract obligations may or may not come from these earnings because these obligations must be paid without regard to whether the enterprise earns a profit.

The correctness of this interpretation is a matter of national public interest. Both the SEC and the state securities agencies spend a great deal of their enforcement resources dealing with novel or irregular securities. By far the most litigated portion of the statutory definition of a security is "investment contracts." Virtually all of these novel securities cases also involve either Ponzie schemes or fraudulent conduct, often aimed

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[2] 15 U.S.C. §77(b)(1).

[3] 15 U.S.C. §78(c)(a)(10).

[4] SEC v. W.J. Howey Co., 328 U.S. 293 (1946).

at the unsophisticated and the elderly. The losses to the general public are enormous.

To understand the size of the problem, it should be noted that, in addition to the SEC, at least 18 state securities agencies have taken action against ETS.[5] When enforcement activities against other payphone operations are added, the number of state enforcement actions rises to over 200.[6] The State of California alone has issued 143 Desist and Refrain Orders against 54 such entities.[7]

These payphone cases are, however, merely the tip of the iceberg. In the past, the agencies have had to deal with similar schemes involving automatic teller machines and other sale and lease-back promotions ranging from rail cars to trailer trucks. *See e.g.*, *United States v. Jones*, 712 F.2d 1316 (9th Cir.), cert. denied, 464 U.S. 986 (1983)(trailer trucks).

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[5]*ETS Payphones, Inc.*, 2002 WL 1586379 (Ind. Div. Sec. June 7, 2002); *National Communications Marketing, Inc.*, 1998 WL 704697 (Kan. Sec. Com. Sept. 25, 1998); *Jerry Klemp*, 1999 WL 20390 (Wis. Com. Sec. Jan. 8, 1999); *Jerome Alex Zanowski*, 2000 WL 1847107 (Ariz. Corp. Com. Nov. 30, 2000); *ETS Payphones, Inc.*, 2001 WL 422179 (Ala. Sec. Com. Feb. 6, 2001); *National Communications Marketing, Inc.*, 2001 WL 236889 (Wash. Sec. Div. Feb. 26, 2001); *Phillip L. Helton*, 2001 WL 1193030 (Mo. Div. Sec. Oct. 2, 2001); *Linda L. Eberly*, 2002 WL 1151509 (Pa. Sec. Com. May 9, 2002); *Gary Randolph Hayden*, 2002 WL 1575117 (Tex. St. Sec. Bd. July 9, 2002); *Robert L. Scott*, 2002 WL 31089631 (Ohio Dept. Com. Aug. 29, 2002); *Department of Banking and Finance v. Mehl*, 2002 WL 31452438 (Fla. Sec. Div., Final Order, Oct. 17, 2002); and *Stigall v. Sec. of State*, Case No:EN-18626 Final Decision (Sept. 6, 2002). The New York and California decisions are reported on the Internet at www.oag.state.ny.us/press/2002/jun/jun12C_02.html, and www.corp.ca.gov/pressrel/nr0016.htm.

[6]Westlaw search, MSEC-CS, payphones /s securities. The search was done on March 11, 2003.

[7]Cal. Corp. Comm'n, Press Release 00-16 (2000), available at www.corp.ca.gov.

This problem will also continue into the future. Ads are presently running on national television, offering similar contracts on both Internet site locations and credit card processing machines. Many of these schemes are advertising that they are the successor to the payphone opportunities!

Beyond the sale and lease-back cases, the SEC and state agencies have had to deal with wide-spread Ponzi schemes involving promissory notes and prime bank frauds. *See e.g.*, *State v. Gerisch*, 49 P.3d 392 (Idaho 2002) and *Mosley v. State*, 253 Ga. App. 710, 560 S.E.2d 305 (2002)(promissory notes); *SEC v. Marino*, 2000 WL 33678041 (D. Utah Oct. 6, 2000) and *SEC v. Pinckney*, 923 F.Supp.76 (E.D.N.C. 1996)(prime bank cases). The states have also been faced with the fraudulent sale of viatical settlement contracts. *See e.g.*, *Siporin v. Carrington*, 200 Ariz. 97, 23 P.3d 92 (App. 2001). All these investments involve either debt interests or fixed return contracts and would not be investment contracts under the Eleventh Circuit's decision.

If the Eleventh Circuit decision is upheld, the SEC will lose its most effective weapon to control and combat these schemes. Further, while the state courts are not obligated to follow federal decisions, they often do. Thus, a huge gap in both the federal and state agency enforcement programs will result. The white collar criminals will have carte blanche to conduct these various schemes with impunity.[8]

The problem will also hamper criminal prosecutions and civil recovery. If the interests are not investment contracts or securities, criminal enforcement actions such as *Szpunar v. State*, 2003 Ind. App. LEXIS 298 (Ind. App. Feb. 27, 2003) can not be brought. Many victims are now able to bring civil securities actions or arbitrations to recover their losses. For example, there

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[8]It is true that many of these schemes are not presently structured to provide a fixed return or the payment of interest. However, such programs can easily be altered to include these features, especially where there is no intent by the promoter to meet these payment obligations.

are presently a number of NASD arbitrations where the defrauded investors have sought to recover their money lost in payphone investments. *See e.g., In re Arbitration: Daugherty and Sowers*, 2002 WL 1944487 (NASD 2002) and *In re Arbitration: Womble and Locust Street Sec., Inc.*, 2001 WL 1636341 (NASD 2001)(both ETS cases). If the Eleventh Circuit position is upheld, using the investment contract theory under the federal securities acts will be foreclosed to them.

Because of the impact of the Eleventh Circuit's decision on both state and federal enforcement activities as well as its impact upon investor recovery, this Court should grant certiorari to review the Eleventh Circuit's decision.

POINT II

THE CONTROLLING AUTHORITIES FROM THIS COURT ARE AMBIGUOUS AND SHOULD BE CLARIFIED

A major reason that the Court should grant certiorari in the present case is that the controlling decisions of this Court appear to be ambiguous. The first case to deal with the concept of an investment contract was *SEC v. C.M. Joiner*, 320 U.S. 344 (1943). The Court in *Joiner* recognized that the definitions of a security found in both the Securities Act of 1933 and the Exchange Act of 1934 are not true definitions.[9] Instead, they are definitions by enumeration. Some of the instruments named in the definition are "pretty much standardized and the meaning alone carries well settled meaning." 320 U.S. at 351. "Others are of a more variable character and were necessarily designated by more descriptive terms, such as ... 'investment contract'...." *Id.* *Joiner* recognized that:

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[9]Nor do the state securities acts which preceded them have true definitions. See the Author's Treatise, 12 and 12A, Joseph C. Long, Blue Sky Law §1:15 (2002)(Hereinafter "Blue Sky Law § ___") for a discussion of the development of the statutory definition.

> [T]he reach of the Act does not stop with the obvious and commonplace. Novel, uncommon, or irregular devices, whatever they appear to be, are also reached if it be proved as a matter of fact that they were widely offered or dealt in under terms or courses of dealing [that] established [them] as 'investment contracts.' Id.

The Court then suggested that whether a device comes within or is excluded from one category of the definition does not prevent it from being included in another portion of the definition. *Id.* at 352.

The Court finally concluded:

> The test rather is what character the instrument is given in commerce by the terms of the offer, the plan of distribution, and the economic inducements held out to the prospect. In the enforcement of an act such as this it is not inappropriate that promoters' offering be judged as being what they were represented to be.[10]

Id. at 352-353. Nothing in the Court's decision hints that fixed return or debt securities should be excluded from classification as "investment contracts."

Three years later, in *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946), again considered what constituted an investment contract.

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[10]This statement is particularly important in the present case because it emphasizes what the investors thought they were getting. In the present case, the contracts were technically cast in the form of fixed payments for rent of the phone. Many of the investors in the present case were elderly. From their prospective, they were making an investment, would receive a return on that investment, and would not participate in the management of the investment. From their prospective, they were buying an investment contract, not a contract for the payment of rent on a payphone.

Initially, the Court made two important observations. First, it noted that the term "investment contracts" was not a defined term either in the statute itself or the legislative history. However, it pointed out the term had been in use for a number of years under the state securities or Blue Sky laws. The Court also pointed out "it had been broadly construed by state courts so as to afford the investing public, a full measure of protection." Then, the Court went on to note that "investment contracts":

> [E]mbodies a flexible rather than static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits. Id. at 299.

The Court, then, announced the now famous test for an investment contract:

> [A]n investment contract for purposes of the Securities Act means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party. Id. at 298-299.[11]

Finally, the Court concluded the scheme in *Howey* was an investment contract. In doing so, the Court stated the essence of both investment contracts and securities in general:

> Thus all the elements of a profit-seeking business venture are present here. The investors provide the capital and share in the earnings and profits;

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[11]The Court restated this test slightly differently:

> The test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others. Id at 301.

> the promoters manage, control and operate the enterprise. Id. at 299.

A security will be present when the capital providing function is separated from the management function. The investor supplies at least part of the capital, the promoter or a third party supplies the management, control, and operation. The remaining two elements of *Howey* further refine the idea. The common enterprise element requires that the enterprise be active rather than passive (such as holding but not developing raw land). The **expectation** of profits element requires that the investment be motivated by his expectation that he will receive a return on his investment.

Again, nothing in the language used or the discussion in the *Howey* case suggests that the profit can not be in the form of fixed payments or interest paid on debt securities. In fact, as the SEC notes in its brief in support of the petition, SEC Brief, p.12, two of the state cases relied upon by the Court in *Howey* involved fixed income or a "guaranteed" return. *See People v. White*, 12 P.2d 1078 (Cal. App. 1932) and *Stevens v. Liberty Packing Corp.*, 161 A. 193, 195 (N.J. Ch. 1932).[12]

In 1975, in *United Housing Foundation, Inc. v. Forman*, 423 U.S. 837 (1975), the Court muddied the waters. The thrust of *United Housing* was to distinguish those cases where receiving a true "profit" was the motivating force behind the investor's investment from those cases where the purchaser of the property was motivated by "the desire to use or consume the item purchased...." 423 U.S. at 852. The Court recognized the *Howey* test and then made the statement which led the Eleventh Circuit astray:

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[12]*See* Blue Sky Law §1:17. For a discussion of the lower federal cases cited in *Howey*, *see* id. §1:18.

> By profits, the Court has meant either capital appreciation resulting from the development of the initial investment as in *Joiner*, *supra*, ... or a participation in the earnings resulting from the use of investor's funds, as in *Tcherepnin v. Knight....Id.*

This statement does not support the exclusion of all fixed rate investments or debt securities from coverage by "investment contracts" for two reasons.[13] First, it is clear from the language used that the Court was referring to its past decisions. As it happens, the Court, at that time, had never considered an investment contract case involving either a fixed return or a debt security. Recognizing that the Court had never had the note problem before it, the Fifth Circuit in *Meason v. Bank of Miami*, 652 F.2d 542, 550, N.17 (5th Cir. 1981) stated that the quoted language "seems to us to be dubious value in [the note] context."

Second, the words "the earnings resulting from the use of investor's funds" turns the *Howey* test on its head. The focus of *Howey* was on the **expectation** of a profit **to the investor**, not necessarily to the enterprise in which the investment was made.[14] In the case of fixed rate or debt securities, the investor makes a profit, even if the enterprise in which he invests does not.

The Court further muddied the waters in *Reves v. Ernst & Young*, 494 U.S. 56 (1990).[15] *Reves* established the test for when promissory notes are securities. However, in footnote 4, the Court made the concept of "profits" more ambiguous by saying:

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[13]*See* Blue Sky Law §2:58.

[14]*See*, for example, *Bell v. Health-Mor, Inc.*, 549 F.2d 342 (5th Cir. 1977) where the investor was to receive a $10 rebate on the cost of his vacuum for every referral made whether the referral bought or not.

[15]*See* Blue Sky Law §2:58, N.11.

> We emphasize that by "profits" in the context of notes, we mean "a valuable return on an investment," which undoubtedly includes interest. We have, of course defined "profit" more restrictively in applying the *Howey* test to what are claimed to be investment contracts. [Citing *Forman*]. . . . Because the *Howey* test is irrelevant to the issue before us..., we decline to extend its definition of "profits" beyond the realm in which that definition applies. 494 U.S. at 953, N.4.

In summary, the Court should grant certiorari in the present case to clear up the ambiguity as to its intent as to the profits element of the *Howey* test. This ambiguity needs to be resolved.

POINT III

THE DECISIONS OF THE COURTS OF APPEALS ON THE ISSUE OF "PROFITS" UNDER THE HOWEY TEST ARE IN CONFLICT

With the decisions of this Court ambiguous over the proper interpretation of "profits" under the *Howey* test, it is not surprising that the decisions of the various Court of Appeals are in conflict. Further, the Eleventh Circuit decision in the present case is also in conflict with other decisions by the Fifth Circuit prior to the creation of the Eleventh Circuit.[16] *See Meason v. Bank of Miami*, 652 F.2d 542 (5th Cir. 1981)(rejecting the district court's holding that an investment was not an investment because the investor was paid a fixed return);[17] *Cameron v. Outdoor*

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[16]In *Bonner v. City of Prichard*, 661 F.2d 1206 (11th Cir. 1981)(en banc), the Eleventh Circuit adopted as precedent all decisions of the former Fifth Circuit decided prior to October 1, 1981.

[17]*Meason* indicates other courts have not been restricted by a concept of a fixed return disqualifying the finding of an investment contract., citing

Resorts of America, Inc., 61 F.2d 187 (5th Cir. 1979); *Bell v. Health-Mor, Inc.*, 549 F.2d 342 (5th Cir. 1977).

The Sixth, Seventh, Eighth, and Tenth Circuits also appear to have accepted the Eleventh Circuit's position. *See Union Planters Nat'l Bank of Memphis v. Commercial Credit Business Loans, Inc.*, 651 F.2d 1174 (6th Cir.), cert. denied, 454 U.S. 1124 (1981); *American Fletcher Mortgage Co. v. U.S. Steel Credit Corp.*, 635 F.2d 1247 (7th Cir. 1980), cert. denied, 451 U.S. 911 (1981); *First Fin. Fed. Sav. & Loan v. E.F. Hutton, Mortgage Co.*, 834 F.2d 685, 689 (8th Cir. 1987); and *Resolution Trust Corp. v. Stone*, 998 F.2d 1534 (10th Cir. 1993).

The Seventh Circuit, however, appears to be willing to reconsider its position in *Hunssinger v. Rockford Business Credits, Inc.*, 745 F.2d 484 (7th Cir. 1984). Of the above quoted language from *United Housing*, the court said "at the time of the *Forman* decision, the Court had not yet considered a debt instrument." 745 F.2d at 491. The court then went on to say:

> As a matter of original principles, however, one may question the wisdom of excluding fixed interest payments from the definition of 'profits.' Congress listed a large number of terms, including the seemingly broad term 'investment contract,' in the definitional sections of the securities acts apparently in order to prevent imaginative promoters from avoiding regulation by inventing nonconventional instruments. [Citation omitted]. It is arguable that giving a restrictive definition to the term 'profits' would be in frustration of Congress's intention. It is of course true that the Supreme Court has strongly indicated that the

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Khadem v. Equity Sec. Corp., 494 F.2d 1224, 1229 (9th Cir.), cert. denied, 419 U.S. 900 (1974); *SEC v. Nat'l Executive Planners, Ltd.*, 503 F.Supp. 1066 (M.D.N.C. 1980); and *SEC v. Weeks Sec. Inc.*, 483 F.Supp. 1239, 1243-1244 (S.D. Tenn. 1980).

> term 'profits' should exclude fixed interest payments, and decisions of this court contain language following the path set by the Court. *Id.*

However, both the Third and the Ninth Circuits have rejected the Eleventh Circuit's position. They hold that fixed return or debt securities can be investment contracts. The Third Circuit in *SEC v. Infinity Group Co.*, 212 F.3d 180, 189 (3d Cir. 2000), stated "the definition of security does not turn on whether the investor receives a variable or fixed rate of return." Similarly, in *United States v. Carman*, 577 F.2d 556, 563 (9th Cir. 1978), the court rejected the defendant's argument that the student loans involved in that case were not investment contracts because the return was in the form of fixed interest and guaranteed by the federal government. See *also United States v. Farris*, 614 F.2d 634, 641 (9th Cir.1979)(promissory notes on real estate) and *United States v. Jones*, 712 F.2d 1316 (9th Cir.), cert. denied, 464 U.S. 986 (1983)(sale and lease back of semi-trailer).

More specifically, two federal district courts, one from the Ninth Circuit, in addition to the trial court in the present case, have found payphone schemes to be investment contracts. *SEC v. Phoenix Telecom, LLC*, 2000 U.S. Dist. LEXIS 22314 (N.D. Ga. Aug. 2, 2000); *SEC v. Alpha Telecom, Inc.*, 187 F. Supp.2d 1250 (D.Ore. 2002); and *SEC v. ETS Payphones, Inc.*, 123 F. Supp.2d 1349 (N.D.Ga. 2000). The *Phoenix Telecom* case had the same type of fixed rental fee agreement as in the present case. As was seen in Point I, the arrangement involved in the *Alpha Telecom* case could have easily been converted to a fixed return agreement.

The Court should grant certiorari to resolve the split between the Courts of Appeals and the inconsistency in the opinions of the Eleventh Circuit.

POINT IV

THE ELEVENTH CIRCUIT'S DECISION IS IN CONFLICT WITH THE INTERPRETATION OF THE SEC, THE STATE COURTS, AND THE STATE SECURITIES AGENCIES ON THE ISSUE OF "PROFITS"

As the SEC notes in its Brief, 23-24, the Eleventh Circuit's decision in the present case runs contrary to the long standing position of the SEC. *See e.g.*, *In re Abbett, Sommer & Co.*, 44 S.E.C. 104, 1969 WL 95369 (1969) and *In re Union Home Loans*, 26 S.E.C. Dkt 1517, 1982 WL 522493 (Dec. 16, 1982).

The Eleventh Circuit's holding also runs contrary to the decisions of many state courts construing the definition of "investment contracts" under the states securities acts to cover both fixed payment agreements and promissory notes. *See e.g.*, *State v. Gerisch*, 49 P.3d 392 (Idaho 2002); *Mosley v. State*, 253 Ga. App. 710, 560 S.E.2d 305 (2002); *Bayhi v. State*, 629 So.2d 782 (Ala. Crim. App. 1993); *State v. Philips*, 108 Wash.2d 627, 741 P.2d 24 (1987); and *People v. Milne*, 690 P.2d 629 (Colo. 1984), all promissory note cases. *See also Manns v. Skolnik*, 666 N.E.2d 1236 (Ind. App. 1996), a contractual obligation to pay fixed return case, *King v. Pope*, 91 S.W.3d 314 (Tenn. 2002), a payphone case with fixed monthly payments similar to ETS, and *Szpunar v. State*, 2003 Ind. App. LEXIS 298 (Ind. App. Feb. 27, 2003), another payphone case.

Several of these state decisions speak directly to the question of whether fixed fees or interest can qualify as "profits." In *Payable Accounting Corp. v. McKinley*, 667 P.2d 15, 19 (Utah 1983), the court said "the critical factor is not whether the rate of return is fixed, but whether the 'investment transaction' is so structured that the money to pay off the investor eventually will be generated by the venture or enterprise."

In *People v. Figueroa*, 41 Cal. 3d 714, 715 P.2d 680, 224 Cal. Rptr. 7119 (1986)(en banc) also addressed the issue of fixed payments, saying:

> Many "investment contracts"...contemplate both a variable and a fixed return. The investment contracts in [*People v. Coster*, 151 Cal. App.3d 1188, 199 Cal. Rptr. 253 (App. 1983)], for example purported to give the investor a 20 percent "fixed" return on principal and 1 percent of the **gross** company income. [Citation omitted.] Both kinds of return, as well as a recoupment of principal depended on the success of the business.... It would be illogical to [to exclude] a promissory note transaction simply because the promised return ... is to take the form of interest at a "fixed" rate. Id. at 740, 715 P.2d at 698, 224 Cal. Rptr. at 737. [Emphasis added.]

Likewise, the state securities agencies themselves have rejected the Eleventh Circuit's approach. As noted in Point 1, at least 18 state securities agencies have brought administrative enforcement actions against ETS. New York has also brought an action against another company offering a similar fixed return plan. *State of New York v. Justin*, 237 F. Supp.2d 368 (W.D.N.Y. 2002). At least two of these state ETS cases were contested cases, and both were decided **after** the Eleventh Circuit's opinion in the present case. **Both** rejected the Eleventh Circuit's position. In *Stigall v. Sec. of State*, Case No:EN-18727 Final Decision (Sept. 6, 2002), slip op. at 13, the Georgia Commissioner said:

> The Commissioner rejects the Eleventh Circuit's analysis of the third element of *Howey* as being inextricably intertwined with its narrow view of "profits." ... [T]he fact that there is a contractual guarantee of payment which might be satisfied from the capital of the enterprise is as irrelevant in this case as it would be in a case involving a

> promissory note. "The statutory policy of affording broad protection to investors is not to be thwarted by unrealistic and irrelevant formulae."

Likewise, in *Department of Banking and Finance v. Mehl*, 2002 WL 31452438 (Fla. Sec. Div., Final Order, Oct. 17, 2002), the Florida Comptroller rejected the Eleventh Circuit approach as representing the law of Florida. He said, "Florida law does not use such a narrow construction of 'profits,' it has not distinguished between fixed or variable returns to the investor."

In summary, since the Eleventh Circuit's position runs contrary to the positions held by the SEC, the state courts, and the state securities agencies, this Court should grant certiorari to examine the issue.

CONCLUSION

For the above outlined reasons, PIABA urges the Court to grant the SEC's petition for Writ of Certiorari.

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